

MINUTES

MONTANA HOUSE OF REPRESENTATIVES 57th LEGISLATURE - REGULAR SESSION JOINT APPROPRIATIONS SUBCOMMITTEE ON GENERAL GOVERNMENT AND TRANSPORTATION

Call to Order: By **CHAIRMAN BOB DAVIES**, on February 8, 2001 at 8:10 A.M., in Room 317-B Capitol.

ROLL CALL

Members Present:

Rep. Bob Davies, Chairman (R)
Sen. Jack Wells, Vice Chairman (R)
Rep. John Brueggeman (R)
Rep. Monica Lindeen (D)
Sen. Bea McCarthy (D)
Sen. Corey Stapleton (R)

Members Excused: None.

Members Absent: None.

Staff Present: Greg DeWitt, Legislative Branch
Mary Beth Linder, OBPP
Cyndie Lockett, Committee Secretary
Amy Sassano, OBPP

Please Note: These are summary minutes. Testimony and discussion are paraphrased and condensed.

Committee Business Summary:

Hearing(s) & Date(s) Posted: Department of Revenue-
Questions & Answers, 2/5/2001
Executive Action: State Auditor

{Tape : 1; Side : A; Approx. Time Counter : 0 - 30}

**EXECUTIVE ACTION ON
STATE AUDITOR'S OFFICE**

Chairman Davies called the meeting to order.

Mr. Brown told the subcommittee he created a history sheet for the State Auditor's Office **EXHIBIT**(jgh32a01).

HB 2 Appropriations

The following motion has been taken to cover all the programs of the agency.

Motion: **SEN. MCCARTHY** moved the base level of funding plus statewide present law adjustments, the additional Governor Martz vacancy savings included in the present law DP 699, the rent reductions in present law DP 698, and general liability premium reduction in present law DP 697, where applicable.

Vote: The question was called for and the motion carried unanimously.

Budget Item: Decision Packages for Central Management

Motion: **SEN. McCarthy** move to approve DP 1 as requested.

Vote: The question was called for and the motion carried unanimously.

Motion: **REP. LINDEEN** move to approve DP 2 as requested.

Vote: The question was called for and the motion carried unanimously.

Budget Item: Decision Packages for Insurance Program

Motion: **REP. LINDEEN** move to approve DP 1 as requested.

Vote: The question was called for and the motion carried unanimously.

Motion: **SEN. McCarthy** move to approve DP 2 as requested.

Vote: The question was called for and the motion carried unanimously.

Motion: **REP. LINDEEN** move to approve DP 3 as requested.

Vote: The question was called for and the motion carried unanimously.

Motion: **SEN. McCarthy** move to approve DP 4 as requested.

Vote: The question was called for and the motion carried unanimously.

Budget Item: Decision Packages for Securities Program

Motion: **SEN. McCarthy** move to approve DP 1 as requested.

Vote: The question was called for and the motion carried unanimously.

Motion: **SEN. Wells** move to approve DP 2 as requested.

Vote: The question was called for and the motion carried unanimously.

Motion: **REP. LINDEEN** move to approve DP 3 as requested.

Vote: The question was called for and the motion carried unanimously.

HEARING ON
DEPARTMENT OF REVENUE

Chairman Davies began the meeting by saying it is no secret that there are problems at the Department of Revenue (DOR). He said people do not envy the subcommittee's job, but he pointed out that sediment to **Kurt Alme**, Director of Department of Revenue. He believed it is the responsibility of the committee to try get to the bottom of these things before they make any decisions on funding. With that in mind he said he would like to ask questions of certain staff of the DOR. He told the DOR they could decide on whoever they wanted to respond to the subcommittee is questions. The subcommittee's biggest issue was with the POINTS System. The information he received through the Legislative Audit Division and other sources that there was a large sum of money unaccounted for. He stated such things as duplicate refund checks based on the fact that POINTS is not working right and because it has problems. He wanted to get into POINTS. In POINTS phase I **Chairman Davies** stated that it is in operation and perhaps the first question should be what does POINTS phase 1 do? What accounts does it handle?

Mr. Alme told the subcommittee that he appreciated the opportunity to address their questions. He said there would be various members from the DOR that are best able to speak to each question. **Mr. Alme** turned it over to **Jeff Miller** to discuss the POINTS phase I in regards to a general overview a what it is supposed to accomplish, and its current status.

He explained generally what POINTS phase I does and what the status is. **Mr. Miller** stated that POINTS phase I was implemented in December of 1999 and they have been operating in the POINTS phase I environment ever since. It is used to transact the department's accounting functions and all revenue transactions flow through POINTS. The information POINTS compiles on a daily basis interfaces with the state's general ledger account system, which is SABHRS. On a daily basis DOR feeds revenue transaction information into SABHRS to allow the state's business to be posted on the books. It also is used for forms and correspondence: 1)it generates mass mailings; 2)it populates forms with names, addresses, id's, and other information. It sends out the forms to their customers so they can be completed and returned to the department for filing. It is also used to manage cases. Cases are any kind of return that rejects while being processed by the system. It is an exception and it is used then to track those exceptions and age those exceptions through the process. This is a module that has been plagued with defects and they have been working through those defects as we have talked about. The Returns processing piece of POINTS is the one that actually takes the information off the return filed by the taxpayer and puts it in the system in a way that there after can keep track of it and compare it to previous quarters and those kinds of things to see if there are any compliance issues. So POINTS phase I as we have try to describe it before is it is the foundation of the entire integrated system it has the modules accounting, return processing, forms and correspondence, case, and utilities module as well. It was put in place as the infrastructure for all the department's business but it is specifically used at this time to process withholding and unemployment insurance. The other cash types will later be added to that foundation.

Chairman Davies asked if POINTS phase II is intended to pick up some of the other things that are not currently in POINTS phase I.

Mr. Miller replied that is correct. **Chairman Davies** asked which ones are those? **Mr. Miller** replied that POINTS phase II will bring on corporate income tax, individual income tax, and the property tax which are the largest tax types. The income and

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corporate tax is one stream of POINTS phase II and the other stream is property tax stream. Both of those are being pursued concurrently.

Chairman Davies asked how are they being handled right now. **Mr. Miller** replies that project is being staged similar to POINTS phase I. It's a development effort that is staged off site of the department's Mitchell Building offices and staged in the Federal Building in rented office space. They have two project teams that are staffed with DOR employees and contractors who supplement DOR's effort. The prime contractor UNISYS and their subcontractors are also there. Those teams work on a very detailed project plan to develop the requirements and test those requirements before they're actually put in place. It's a build effort that is occurring as we speak.

Chairman Davies asked is POINTS phase II totally inoperable at this point and where are you feeding the information on individual income tax, corporate income tax, and property tax if POINTS phase II is not working. Mr. Miller said the present individual income tax, corporate license tax, and property tax, are operating on the system called legacy systems. Legacy is not a name brand. It's nothing else but being old systems that have been in place for a long time. The income tax and the corporate tax systems collect revenues associated with those taxes and actually interface with POINTS phase I now because they're used for accounting and financial transactions. So there is a interface present.

{Tape : 1; Side : B; Approx. Time Counter : 0 - 30}

Sen. McCarthy stated that \$17.8 million was spent on POINTS phase I. **Mr. Miller** told **Sen. McCarthy** that with POINTS phase I the contract that they had with UNISYS spent \$11.3 million. They did spend the \$3.8 million that was associated to building the revenue and information processing center and reengineering the department of revenue and that was also a part of POINTS phase I.

Sen. McCarthy asked if POINTS phase II is an additional \$18 million and if this goes toward the system that is not working.

Mr. Miller said POINTS phase II is funded at \$18 million, but the reason it's not working is because it's underdevelopment and it has not been attempted to be put in place. It's not ready to be put in place. It will not be put in place until later in the calendar year, in fact, this fall of the calendar year. It's not a question of not working it's a question that it's under construction and not ready to be implemented.

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Sen. McCarthy asked if they all ready spent \$10 million of the \$18 million.

Mr. Miller said no that is not correct. They signed a contract with UNISYS for \$10 million to develop POINTS phase II of that amount they have spent roughly \$3 million to date with UNISYS. We have spent additional money out of the \$18 million authorized to hire private contractors that supplement this effort. He believed that he reported to the subcommittee previously that of the \$18 million authorized by HB 15, they have spent to day \$6.26 million and of that amount we have spent roughly \$4.3 million with UNISYS. The reason that amount is a little larger than what he said before was because there was another phase to the project. The total with UNISYS to date is \$4.3 million: \$1.8 million for local contractors, and \$9.8 million of the balance encumbered under contract. They do expect to spend what they have encumbered and expect to spend all but \$2 million of the \$18 million. That difference of \$2 million of that not encumbered is money they are reserving to make sure they do not release the contractors from this project until the project is stable.

Sen. McCarthy tries to clarify by saying the DOR had \$2 million left of POINTS phase II money and they have approximately \$6 million left over from POINTS phase I money. **Mr. Miller** said we should go from the top again. He stated of the \$18 million they have spent \$6.26 million and that leaves a balance of roughly \$11 million. Of this amount \$9.8 is encumbered (by that he means they are obligated under contract and are expected to spend).

Sen. McCarthy said you would have \$1.5 million left over then.

Mr. Miller agreed and stated that with regard to the \$17.8 million, all but \$495,000 has been spent.

Rep. Lindeen asked with the original contract with UNISYS to implement POINTS phase I, in Appendix B of the information supplied by the DOR, it states that the warranty period ended in August of 2000. So was that for both Phases or just for POINTS phase I and, if so, what is the warranty period on POINTS phase II. **Mr. Miller** replied each of these projects have phases and once they go through an acceptance phase then there is a warranty phase. In POINTS phase I, that warranty phase was 130 days beyond implementation. At the end of that period, the DOR was not satisfied and they complained to UNISYS. DOR was not pleased that UNISYS did not provide the closure they expected on some of the defects. As a result of this complaint, the warranty phase was extended at no cost to the DOR. UNISYS absorbed the cost of the warranty extension.

Rep. Lindeen asked what was the extension after the first warranty had expired? **Mr. Miller** replied it was a six week extension and UNISYS contributed staff and extended their commitment for an additional six weeks beyond the original expiration date. **Rep. Lindeen** read some of the information supplied by DOR and stated that many of the defects that occurred were considered mission critical. They're were an incredible amount of defects of which only about 25 percent have been resolved and they are way passed the six week extension. **Rep. Lindeen** then asked how the department is handling the defects now? **Mr. Miller** said they are handling it with contracted programmers and DOR programmers in a maintenance phase under POINTS phase I. They are continuing to work through a back log of defects associated with POINTS phase I. They do that in a prioritize manner so the warranty did not solve all the defects and they are left with many defects they are working through.

Rep. Lindeen asked if there were that many defects concerns, and problems, why was there not more of a push for a longer extended warranty. **Chairman Davies** rephrased the question. He stated that he understood the DOR signed off on POINTS phase I and he assumed that the warranty ran from the time the DOR signed off. **Mr. Miller** agreed with Chairman Davies. The real question from **Chairman Davies** was, did the DOR sign off on POINTS phase I prematurely? **Chairman Davies** stated that he had a whole list of problems and he was going to read some of them.

Last year the computer system was unable to process any refund checks until the last week in January. Over 3000 taxpayers had their checks sent to the wrong address. POINTS used the previous years address for those taxpayers regardless of what their return said and many went to addresses that had nothing to do with the taxpayer. Some taxpayers never received checks even though the system said that they did. This fall when the errors were found, most checks were sent out without the 9 percent interest required by law unless the taxpayer called to ask for it. This defect may still exist in POINTS and occur again this year. Hundreds of taxpayers received duplicate income tax refunds last year. There were some days when every check issued had a duplicate sent, as well. The department has not identified all those taxpayers yet. Many returned the duplicate checks, but not all did. Thousand of payments that were posted to the wrong account were entered incorrectly by a scanner, which was discarded by Wisconsin and purchased by DOR. Yet when staff took carts full of examples to show the department the process lead over the data input process did not show up for the meeting and the lead in charge of the section said that their concern was getting the money in the bank regardless of how it was done. She

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refused to look at the examples and told them they would not be responsible for fixing the errors. Duplicate refund checks were issued to 231 corporations. Many individuals had offsets for child support taken from their checks even though they were current. Some CPA's received checks that were written to them for the exact amount of their client's refunds and the clients received a check as well. This happened in cases where the CPA's address was on the address label of the tax return. As of January 2000, there still were 15,000 returns for 1998 that which had not been processed and the returns had to wait for over a year. Testing for electronic filing is not completed until late in the season and major tax firms like H & R Blocks and large CPA firms could not e-file their Montana returns (e-file returns piggy back on the federal return so the federal and state return are submitted simultaneously or can't be submitted at all). Therefore they had to process paper returns for an unknown number taxpayers who might have e-file, this slowed the refunds and cost processing time. Hundreds of accounts were assessed and payed a 10 percent service charge. It was later found to be erroneously programmed and this fee of 10 percent was to be added to all accounts that were over 41 days pass due and the charge based on the total tax penalty and interest. It has not yet been refunded. Although leadership said they are planning to draw up procedures to do so. **Chairman Davies** said he will stop at this point in the list, but he stated that the customers out there are generally tolerant when a mistake is made and they accept that. The volume of problems reflected here is certainly a problem and again his question would be, if these problems existed was POINTS phase I signed off prematurely. Were the legacy that kept in operating parallel as it would seem appropriate to do on a new system like this.

Mr. Miller addressed the first question regarding POINTS phase I being signed off prematurely. He stated that DOR signed off on POINTS phase I in 1999 in part because they were up against Y2K issue. This system was to be the solution to the Y2K issue. DOR tracked all through the process to determine if this system should be a go or a no go. They tried to figure out if they should maintain the old legacy systems as the year approached or put all their eggs in one basket with POINTS phase I. In the end, they decided to go with POINTS phase I and as they look back on their decision they feel it was a very turbulent decision and has caused much difficulty. DOR does not deny they have had difficulties implementing to the level of continuity and success they would like. They expected when they signed off that the defects would be covered in warranty and when the defects were not resolved DOR went to UNISYS and said they were not satisfied. UNISYS's solution was to extend the warranty and this solved some problems, but discovered more. In the end, DOR excepted POINTS

phase I before it was thoroughly tested. DOR recognizes now that was a mistake, that was not a mistake that we intend to even go through with POINTS phase II. The contract criteria for POINTS phase II is different then what DOR accepted in POINTS phase I. DOR will not accept the contract unless its running like it was designed to run. They have learned from that lesson and it has caused some turbulence and it has caused the errors that **Chairman Davies** has identified. The errors are being resolved and fixed. DOR has gone back to those taxpayers and tried to help fix their problems.

Sen. McCarthy asked how DOR is handling the duplicate checks.

Mr. Miller told her that they cancel one of the checks or asked the taxpayer to send one of them back. **Sen. McCarthy** asked if there was a count on how many checks are still out there. **Mr. Miller** said he would have to do some research on that because it didn't have it with him. **Mr. Miller** said **Neil Peterson, Process Lead of the Customer Service Center**, could discuss the specifics on the refund checks. **Mr. Peterson** told the subcommittee that he believed the number of duplicate checks was around 495 plus or minus two or three. He stated they know when they send duplicate checks and have a handle on it. As soon as they knew they had duplicate checks they sent out a letter to all the people who got a duplicate refund check and asked them to send back one of the checks they had not been cashed. If they did cash it they were instructed to send the money back. **Sen. McCarthy** asked how many out of the 495 duplicate checks the department has not received back? **Mr. Peterson** said there was a handful, like 10 or 12. **Sen. McCarthy** asked is there any legal way to get the money back from this years return. **Mr. Peterson** said yes and for the folks who did not send the money back there is a receivable in that persons name. This year's return can be confiscated and the portion owed will be taken from the refund.

Rep. Lindeen asked about the warranty and how could there be a premature sign off on the warranty. **Mr. Miller** said what happens was there were detail steps in this project that lead up to exception and those were testing kinds of things. Once there was acceptance the warranty starts and in this instance, once DOR accepted there were 22 days with the contractor's staff working side-by-side with DOR through the implementation steps. At the completion of the 22 days the contract started a 130 day warranty. This meant UNISYS provided contract staff to work with DOR at their direction on whatever issues DOR choose to assign them. **Rep. Lindeen** said it seemed to her until all bugs are worked out of POINTS phase I it is impossible to implement POINTS phase II. **Mr. Miller** said it is a very legitimate concern and very serious concern. Right now DOR has in place a business

coordination team and a configuration management team so from the business side DOR has users looking at the design of POINTS phase I and these are the changes that need to be made to accompany these other taxes coming into the environment. They will make sure it's coordinated and reconciled. At the same time, we have the technical-folks the programmers that are doing this from a configuration management perspective. These programmers need to reconcile what is in POINTS phase I with what is now going to becoming POINTS phase II. POINTS phase II is planned later in the year and between now and then we need to fix the defects and make sure the system is stable.

Rep. Brueggeman asked if POINTS phase II is allowed to go forward, does DOR plan to run POINTS phase II parallel with the old legacy system. **Mr. Miller** asked **Denny Espeland, Department of Revenue POINTS Project Manager** to answer. **Mr. Espeland** said they do not plan to run parallel in the production environment, because its very challenging and duplicates the work the users have to do. What his team has done for implementation in POINTS phase II is add three testing phases. An additional phase was the conversion phase, because one of the biggest problems they had was that it worked relatively well with clean data, but when they entered data off the old system it was not as clean and it caused problems with the system. The other two phases are the acceptance phase and system testing phase, which is conducted by the contractor. The last two phase are performance testing phase and the most important phase is aggression testing phase. The regression testing phase is the most important and is simulated testing of production data. His team is also using production scenarios in other words they take live production data and run it through these scenarios. **Rep. Brueggeman** asked how many mission critical errors does POINTS phase I have? **Dan Ellison, Information Technology Process Leader** that as of today, there are 183 mission critical defects in the four modules of POINTS phase I. **Rep. Lindeen** said POINTS phase I has gained more mission critical errors since the last meeting. **Mr. Ellison** said that new defects have been identified since the last update and they have been tracked and assigned to their programmers. They are being worked as they were speaking. **Rep. Brueggeman** asked if the department had a time frame on when these errors will be resolved. **Mr. Ellison** said he could not give a specific date or time frame when all the errors would be resolved. He said they are doing their best to resolve them and they have a total staff of 17 people working on POINTS phase I including maintenance and defects. Management is very much engaged in overseeing that effort and they will continue to do that to the best of their ability. **Rep. Brueggeman** asked if the legacy systems would have failed in the Y2K environment?

{Tape : 2; Side : A; Approx. Time Counter : 0 - 30}

Mr. Ellison said there would have been some investment required to get the legacy systems Y2K compliant. If the decision would have been made not to implement POINTS phase I **Mr. Ellison** said he could not give an accurate answer on what it would have taken to get the legacy systems up and running.

Rep. Lindeen wanted to go back to the original contract and asked who made these decisions. When the decision was made and maybe we talked about this in previous meetings, but when the decision was made to contract with UNISYS who looked at the contract, who was involved in making that decision, and did the contract include specific phases that would be tested. The additional phases now included in POINTS phase II now should have been included in POINTS phase I and why were they not? Who would have allowed that to occur? **Mr. Miller** said the decision to sign with UNISYS was very detailed analysis of an RFP process of proposals that met specification requirements. DOR went through the three proposals and only two of the proposals presented viable options and DOR chose UNISYS. **Rep. Lindeen** asked who made the decision and **Mr. Miller** said it was a committee process. Committee evaluated the RFP, with some assistance from the Department of Administration (DOA). He also said the Information Service Division of DOA assisted in evaluating the RFP proposals.

Sen. Wells asked about material that the subcommittee was given in response to the LFD Issue regarding the first question on lack of performance measures with POINTS. He talked about the financial benefits of POINTS and the revenue lift. He stated if everything was running smoothly and were no defects, then maybe these financial benefits of POINTS would be true. But have they figured out the financial benefits of POINTS right now or made some projections that include the problems. **Mr. Miller** said that business case or financial look was based on the revenue lift described and did contemplate a smooth running system. It also contemplated that there would be a phase approach to brining the various tax types into the system. Now we did not contemplate having 183 mission critical errors. DOR is confident that when those defects are resolved, and they intend to resolve them, that they will see the revenue lift. It may be an issue of timing but again the financial benefit shown there is trying to point out that the cost of developing this system and including the interest on the bonds that will be paid will be more than offset of the revenue lift that DOR expects. **Sen. Wells** asked how much additional cost is DOR talking about to resolve these defects when DOR is putting together teams of programmers to troubleshoot these unexpected problem areas. How much of an effect will this

have on these figures? **Mr. Miller** answered those figures are predicated on the full amount of bonding money being spent and DOR is continuing to operate under the budget created for this project. DOR has \$17.8 million in the first issue of bonds and an additional \$18 million. The expenses that occurring are still projecting below that bonding limit. DOR has not even committed, under contract, the full amount of those bonding proceeds. Yes, the continuing expenses were contemplated in the sense of having to supplement DOR's resources to keep up the contractor and so forth. What was not planned for were 183 mission critical defects, but DOR continues to work within the funds that was authorized.

Rep. Lindeen asked if the State of Montana has a process that adequately develop and administer large information technology development projects? **Mr. Miller** stated that in his personal opinion DOR has attacked this the best way they were able and has drawn the best talent we could get. DOR hiring outside assistance, because DOR knew they did not have it in house.

Mr. Alme wanted to address **Rep. Lindeen's** question. He sees two issues here. One is trying to expect the unexpected, which to a great extent in this environment DOR has not been able to do. The second issue is, does DOR have control procedures in place that allows DOR to deal with the unexpected that seem to be inevitable. That is what DOR has tried to do in POINTS phase II and that is what they continue to do to internally review the internal procedures to see if DOR is in the best position to handle the unexpected. DOR has been trying to keep the subcommittee apprize of all the things that are going on and this week DOR was given another issue that was unexpected. **Mr. Alme** stated that on Tuesday the prime contractor reported that an issue with their subcontractor would suspend Development work on a portion of the property tax system. This is an issue between the prime contractor and their subcontractor. It becomes an issue, with the DOR because they have contract procedures in place that involve how DOR is to handle resolution of this kind of issues and to anticipate that this will be the last one. **Mr. Alme** stated they would work with the Legislative Auditor to address the issues that need to be addressed and to get the issues out in the open. He stated that he could not stand before the subcommittee and tell them that he knows for certain what will happen with this project. He can not say wether it will get done in a certain period of time and at a certain cost. This project has a lot of unanticipated turns and twists. DOR has an internal committee constantly evaluating the risks and the benefits versus the costs and where the DOR is and where it is going in the future. **Mr. Alme** assures the subcommittee that DOR

is doing that and if the subcommittee has any other questions that they can answer about their internal control procedure, how they monitoring the problems, and issues on a go forward basis he would again be happy to share that information with the subcommittee.

Rep. Brueggeman asked if there's a feeling among the DOR staff that the mission critical defects could be solved within the biennium? **Mr. Ellison** said before when DOR last met with the subcommittee that they had significant defects in the accounting module, which is one of the most critical modules in POINTS phase I. They are focused on the mission critical defects in the accounting module and they established a time line of middle to the end of March to try to have those defects resolved and to move those defects into corrective action, do the aggression test, and move them into production. This will allow the users to have these functions available to them. This, however, will not clear the defect list and they expect that between now and the end of March more defects will be generated. DOR is working hard to try to get on the front side of the curve so they are fixing more defects than those that are being generated. He felt they were at an equilibrium, but would have to watch the trends closely. They can report back to the subcommittee on a monthly base on how things are going. **Rep. Brueggeman** asked how many of the mission critical defects apply to the accounting module. **Mr. Ellison** said 45 defects in accounting module since November-December apply to the accounting module. There have been new accounting defects generated in the time between when they sent the report to the subcommittee and today. For the record, the subcommittee can refer back to Appendix B and the numbers were good numbers when they gave those reports to the subcommittee. **Rep. Brueggeman** asked if it's appropriate to piggy back another system, POINTS phase II, while they're still working on POINTS phase I because it is basically failing. Is it in the State's best interest to go ahead with POINTS phase II? **Mr. Ellison** said that is a very fair question and DOR has looked at it pretty much on a weekly basis when they get status reports on the POINTS phase II development effort and then they look at what is happening with fixes to POINTS phase I. **Mr. Ellison** said he would not be able to give a final answer today it's prudent to proceed or not to proceed, as the subcommittee knows they are well along the track of development in POINTS phase II for the individual income tax, corporate tax, and property tax modules. This is something DOR can certainly assess and bring back to the subcommittee at an appropriate time.

Rep. Lindeen asked, based on the fact that there are still 45 defects with the accounting module, how can the legislature be

sure that the revenue information that DOR has received and continues to receive is accurate and that the data can be relied on to make good budget decisions? **Lynn Chenoweth, Resource Management Process Leader**, said the current status of POINTS will give accurate data from a revenue standpoint. **Mr. Miller** echoed what **Mr. Chenoweth** said that DOR is very confident that the total dollars collected for income tax and corporate taxes and other kinds of taxes are being correctly recorded in POINTS. The confidence of the accuracy at the customer level is the defects that are holding DOR up from issuing some statements of account. Although they are confident at the global level that's less reliable and they will not act on it. DOR has information coming out of the customer level. These defects are not impacting the money coming in, but are impacting the ability of DOR to service the individual customer. DOR is not confident the calculations are right for the interest and penalty. Because they are not confident they will not act on that information until they are certain it's right. They know that the total amount was put into the right accounts and that it's correctly reported up to the State general ledger system.

Sen. Wells would like to hear from other people and the **Chairman Davies** suggested we open the meeting up to comments.

Rep. David Wanzenried House District 68 in Missoula, discussed his interest in the DOR issue since he appeared at the General January 19th, 2001, Government hearing. He does not want his comments to reflect on the individuals of the DOR who have commented this morning. He feels that DOR has dedicated individuals doing their job, but from his assessment of what has happened he feels that it can not continue with business as usual. **Rep. Wanzenried** said it's necessary to look at where DOR is in this process. The information given to the subcommittee is accurate as far as it goes. His perspective is that it's not only a DOR problem but the legislature's problem. Not just as legislators, but as taxpayers, customers, and consumers. He drew the subcommittee's attention to the fact that DOR moved to POINTS phase I prematurely. They did that because Y2K was a concern for the legacy systems. Was it cost effective?. He has not seen any documents on the costs required to upgrade the legacy systems to address the Y2K problem. If DOR is going to make a decision with all those risks associated with running a system by itself that is new, then DOR should have done their homework. There is no evidence, to his knowledge, that has been presented to anybody that indicated the reason for abandoning legacy because of those problems. He will stand corrected if DOR can provide the subcommittee with that information. He reiterated that the legislature has committed \$32 million in bonding authority for

POINTS phase I and POINTS phase II. The SABHRS system does the accounting for the State of Montana and cost \$16 million, so this is a lot of money here. He submitted to the subcommittee that one of problems is that system commitments are made without the requirement for third party quality assurance to ensure the kind of questions that the subcommittee is addressing get taken care of early on in the process. There is no available resources in the state government to do this so they contract for it. For investments of this size there should be someone to guard the investment and to be a watch dog for the legislature especially if there is no resources internally. The evidence brought before the subcommittee today indicates there is no expertise and its not under contract. If the legislature does any changes with information technology that by itself should be addressed. He wants the subcommittee to look at the copy of the report dated January 31, 2001. This report would lead the subcommittee to believe everything being done now is ok. One of the points made is that the State of Montana's comprehensive annual finance report has been adjusted to account for the misstatements and the state's financial statements are properly stated. This is right, but the DOR has not been audited. In order to do the report the Legislative Auditor has to be able to audit the activities at year end to certify that the statements were properly accounted for and that DOR has been audited. At the end of the calendar year 2000 there were 50,000 cash transactions that could not be accounted for. The Auditor can not audit the information that DOR has stated. That's a problem, because for the first time in 15 years there can not be a certification and an issue of the report that is usually done by November. There is no certificate of achievement for having done this in a timely and accurate manner. It cannot all be related to POINTS because SABHRS plays into this. However POINTS is a big part of the problem. **Mr. Wanzenried** suggested to the subcommittee that they can not look at it as a DOR problem. It's a bigger problem than that and the legislature needs to make certain before they leave the session that the legislature address significant policy questions. This could affect the states bond rating.

{Tape : 2; Side : B; Approx. Time Counter : 30 - 60}

Mr. Wanzenried mentioned that on page 2 of the report it talks about the fee overstated income tax and corporate tax collections of by \$18 million. The response was that it is not anything new and everyone knew about it when they did the audit. The problem is there was not sufficient internal controls that the overstatement of revenue was found by the DOR. It actually posted in the SABHRS system and was discovered by the Legislative Fiscal Division. \$18 million is a lot of money and he is not sure

if the cause of the problem has been corrected. There is no way to continue to operate on the premise that they will take care of this. It looks like there are three problems here and they are all interplaying with one another in a negative way. There is a hardware problem, software problem, and a personnel problem. The most significant one the subcommittee has talked about is the software problem. Personnel problem comes from the reorganization done by DOR during which a lot of the senior personnel simply left. The legislature will be relying on other information that DOR will be providing for revenue estimates for not only the general fund, but every other revenue source. The director of DOR has asked the Legislative Auditor to do a performance audit of DOR and specifically to take a look at POINTS. The Legislative Auditor will not get to that until sometime in July and the legislatures will be long gone and they have a lot riding on this. If his math is right there is less than \$500,000 left in the \$14 million investment that was supposed to take care of the implementation of POINTS phase I and he is certain the DOR response is that they plan to carryover it over and cover part of those costs in POINTS phase II. When it is all done, how much more is it going to cost the state to finish straightening out POINTS phase I. The next issue is, if DOR brought in all these employees to work on this environment what tasks that they normally are assigned to are not being performed. How many employees are working on this BLITZ? If they were not working on this what would they be working on? The subcommittee is going to be asked to act on the Executive Budget next week and what will the money be spent on. Will the legislature spend it to do POINTS or spending to do programs that agencies are telling the subcommittees they need. One problem he feels is the information technology plan is not a plan, but a promotion. It is an advertising manual to tell us everything is fine. He looked at what POINTS was advertised to do. They said it would do all the things that everyone has addressed, but does not work right now. He knows when there is an undertaking like this you do not plan on it working perfectly, but when the legislature is asked to fund these projects no one says there is a high probability of risk that it might not work. **Sen. Wells** said the premise was that it was going to generate additional revenue. **Rep. Wanzenried** mentioned two other points to the subcommittee. The Department of Labor and Industry is an integral player in this decision. They are totally dependant on POINTS phase I to process unemployment insurance. The premiums that are due through the state have to process through this system. **Rep. Wanzenried** told the subcommittee he has talked to the Department of Labor and Industry and **Mr. Alme** and this is a low priority right now for the Department of Revenue. This a problem because if the subcommittee reads the Legislative Audit

it will find that Montana was late making payments to the federal government for significant sums of money. Those payments were do with interest paid by the DOR. The money come from the general fund. He states that the legislature need to do more than simply say yes we trust you and please work at this real hard, because we know these folks will do this and we know some of these folks personally. There is too much at stake here and the legislature will not be around if things don't workout. It will be expensive to make these mistakes and errors and legislature will have to deal with it 2 years from now. He pointed out the Customer Service Center was set up as a proprietary account and was off budget. He told the subcommittee that DOR wanted to be a proprietary account, they will set up like a business. DOR projected volumes they were going to do with other agencies and internally. **Mr. Wanzenried** found out that DOR never talked to other agencies and got information they could actual use as a Customer Service Center. But this was predicated on POINTS working to take care of the accounting needs that the other agencies had. Those agencies did not use the Customer Service Center. DOR had to borrow \$1.2 million to cover the costs. He stated that he is in the private sector like most legislators and if he had revenues not coming as budgeted he would reduce overhead and fixed cost. When the workload and the demand for services didn't materialize the DOR kept spending money as though they had money and then had to get an interagency loan to cover those costs. If you do not require the DOR to pay that out of its own budget then it becomes a supplemental appropriation that everyone will have to pay for. There are also indications in the Legislative Audit report about \$4 million in general fund that was used to supplement the cost associated with the POINTS. Maybe someone from the Legislative Audit Division can talk about that. **Mr. Wanzenried** said that legislators need to respect the fact there is separation powers and not tread upon the prerogative of the executive, but at the same time there has to be some accountability on the executive's part. Legislature authorizes these expenditures and they will authorize more. The directive should be that the legislature should not proceed with POINTS phase II until POINTS phase I is completely operational and that these mission critical defects and others defects are taken care of. It is important because POINTS phase II assumes POINTS phase I is working and DOR is committed contractually to contractors to do POINTS phase II. If the legislature decides to pull away from the contract then they will face a penalty to get out of the contract. There needs to be a greater emphasis on the Department of Labor's problem. That is an important issue because if the legislature decides to proceed with the Customer Service Center and it is the only user of POINTS, then the transaction fees will have to up. Federal government provides funding for administrative cost to administer unemployment

insurance trust fund we have. This trust has increased by about \$10,000 in the last five years. The transaction costs are going to have to go up significantly if the user base stays small and at some point this will become a problem for employers in the state. They will have to pay the cost of supporting the contract between the DOR and Department of Labor. Department of Labor is not comfortable with their position because they can not go anywhere else. This problem can not be simply confined to the DOR. The problem goes beyond that and everyone must respect the decision the subcommittee has before it. The decision needs to reflect, that changes have to be made in securing the design, installation, and evaluation of these systems by a third party contractor. It just does not seem to be working the way the agency is go about it right now.

Sen. Stapleton said many of these third party contractors seem to be a part of the problem. These are people who don't understand the different agencies and how they work. He felt that **Chuck Swysgood, Director of Budget Program and Planning**, wanted the subcommittee to forgive the debt and move back the Customer Service Center (CSC) back to HB 2. How is getting more people outside the system going to help? It failed in the past and why is it with the leadership we have now that it can not help. **Mr. Wanzenried** said he was not sure that he could say that a third party quality assurance would work any better than what was already in place. He would like to think conceptually that it is an idea that would be looked at, because it is clear without someone under contract to evaluate progress being made and to advise the department on how to hold people accountable that the problem will not go away. He gave the example of the DOR and if it was wise to do the warranty. **Sen. Stapleton** said he can tell that DOR did not work with other government agencies to get a buy in for using the CSC. In other words there was that understanding that this was going to be a Customer Service Center for Helena government. **Mr. Wanzenried** said DOR just did not contact the other agencies and get a commitment.

Mr. Alme thanked the subcommittee for approaching the issues constructively. DOR is certainly interested in working with the subcommittee and legislature in trying to be sure they effectively administer the DOR. He asked that before the subcommittee makes any dramatic funding changes that will impact how DOR will go forward that the subcommittee will include the DOR in their discussion. DOR will be sure to get all the facts out to the subcommittee and be a part of that process. He would like a chance to respond to any of the issues that were raised by the subcommittee, the auditor, and by **Mr. Wanzenried**. He would like to clarify that the CSC and how it happened from a revenue

point of view to the general fund. It is not a hit of \$2.8 million on the general fund due to the CSC. DOR has another analysis on the CSC and how they got their technically. One last thing he stated was his experience with the people of the DOR and how impressed he is with the initiative the department has taken to try to make the DOR more responsive and cost effective.

{Tape : 3; Side : A; Approx. Time Counter : 0 - 30}

Rep. Lindeen asked about the \$3.0 million used to supplement the CSC. **Mr. Miller** said that it speaks to the first year of experience with the Customer Service Center. They did not have rates for every activity that was performed on behalf of the department. They paid them everything they were authorized to pay even though they did not have in place a billing mechanism to account for every activity that they did. DOR was appropriated in HB 2 budget monies to pay CSC. In the Legislative Audit report pointed out what is supposed happen and DOR acknowledged those billings procedures were not in to place. The DOR paid for the full amount of services. They made payments that were not supported by direct billings.

Sen. Stapleton asked about LFD issue number 6 on page 10 and how these results went down in the fiscal year 2000. Revenues were \$9 million lower and were directly related to the number of audits completed. Is this a result of DOR focusing their attention on solving the problems of POINTS and directly causing the loss of millions of dollars of audit revenues that DOR is not doing. **Mr. Miller** said there are three reasons for this decline. First, key staff are being diverted to this new computer development and this creates vacancies and other people have to pick up the slack. Second, the computer system is not operating like it was intended and does not allow DOR employees to do things in an automated fashion they would normally do. This has inversely impacted the DOR collection activity. DOR also knew there would be some risk and they didn't want it to be more disruptive than necessary. DOR has been trying to manage the affect and develop workaround and other solutions that get them through the day-to-day business they need to do. Third, is the DOR has a bad time recruiting auditors. They have been in a recruiting mode for better than two years and presently have very high vacancies in the auditor ranks.

Sen. Stapleton asked **Mr. Miller** if he would want to work for the DOR right now. **Mr. Miller** replied yes and because it is very interesting work. The salary situation is very serious. **Sen. Stapleton** asked what **Mr. Miller's** thought was on the cost benefit analysis for this revenue being lost due to the audits. **Mr.**

Miller replied this money is not forever lost. DOR has a statute of limitations within which the DOR is supposed to conduct audits before the year closes and drops off. So there might be an interruption now, but they have not lost all this revenue. **Sen. Stapleton** said that they need to keep current with these audits. **Mr. Miller** said it is collected through the accounts receivable.

Lisa Barton, Income Tax Field Auditor for the Department of Revenue in Billings, commented that she has had an interested in POINTS from the start. She stated that bad things can happen to good government and the report she gave **Chairman Davies** are the facts she found out about the DOR. She has been learning about other governments and what is happening to them through the website for the State of Mississippi (mstcstate.ms.us.). Mississippi tried to implement an integrated tax system and got five years into the system. They only put on withholding tax just like Montana and a contractor and their best people. Mississippi lost revenues of \$299 million and they were able to sue because they did not sign off on the warranty. They received a short letter of apology and check for \$185 million. She said that it is not a matter of \$4 million or \$32 million, which is a God awful amount to spend on a program. She said it is not only the budget money that will come to the DOR that is at risk, DOR is risking the collection and administration of the income tax, property tax, and payroll tax. As of today there are 35,000 payroll accounts and 260,000 review items. Review items are mistakes and some of these adjustments take 35 to 45 minutes each to clear up. When she looked at combination taxes since November of 1999 the DOR does not know who has not sent in a third reports and who sent in coupons. The DOR is not doing what the subcommittee and taxpayers have intrusted us to do. We must administer the tax laws of the state. The managers of DOR are good people with well intentions. They are probably mad at her right now, but the DOR has a public trust. She is concerned when she looks ahead and sees that they say are going to put income tax, which has 480,000 accounts, on to a system when they can't even account for the 35,000 payroll accounts already. She asked the subcommittee to be objective and look at the risk. If the DOR puts the property tax system on to this system it is going to be a train wreck. On July 1 DOR has a legal obligation to turn over taxable values to the 56 counties. The taxable values produce over \$990 million of revenues that fund the state's schools, fire districts, and sewer districts. DOR has not sent out statement of accounts for several months. Property tax people are coming up on a reappraisal of 900,000 parcels. She's risking her job to identify a problem because there is a difference between a bureaucrat and public servant. Public servant looks at the person across the desk weather it is an

employer and they have an obligation to that person to do their job the best way they know how. Montana does not have an economy that is going to withstand a loss in revenues to the state of \$300 million in five years. DOR just doesn't have 15 months of time invested in this computer system, they have 3 years. But the best thing DOR can do is take a look at what has happened to other states. She called Denver and talk to a programmer there. The programmer said the code was bad from the beginning and said it is been three years into the sales tax. The worst thing they did for moral and his auditors are doing data entry. He was not sure what was lost in revenues. UNISYS asked Denver if they would be a model for other customers. He said no. **Mrs. Barton** explained other scenarios that she researched. The State of Florida had problems with UNISYS also. She said she goes into the businesses she audits and 70 percent of the time she is apologizing for the DOR for mistakes made by the system that she has to correct. She gave the subcommittee information in handouts **EXHIBIT(jgh32a02)**, **EXHIBIT(jgh32a03)**, **EXHIBIT(jgh32a04)**, **EXHIBIT(jgh32a05)**.

Chairman Davies asked about making a hard decisions and asked if POINTS phase I is beyond salvage. **Mrs. Barton** said that there needs to be an evaluation that talks to people who have been through problems with UNISYS. She does not want the DOR to lose anymore revenue. She said Idaho had a system called Jentax, which is an off the self product and it works real well for them. She said she does not want the DOR to run out and buy it but feels that there needs to be a deadline for getting POINTS phase I fixed and this needs to be done before to much more money is spent.

{Tape : 3; Side : B; Approx. Time Counter : 30 - 60}

Rep. Lindeen asked if she could get more information about UNISYS and what states they have worked with and information on the bad code. **Mr. Miller** said the DOR will put that together for her.

Chairman Davies said the DOR was under pressure trying to get this system up. **Chairman Davies** commented about a situation he was in with the Minutemen Missile System and when they had problems with that the answer was to bring more and more people on. More people translates into more money. A person mentioned to **Chairman Davies** that at one point these DOR development people were doing work at home. They were charging almost 80-90 hours per week of overtime pay. He would like that addressed by DOR. Maybe some overtime records could be provided to see if that is a true comment or not.

Clayton Schenck, Legislative Fiscal Division, made a comment that this situation is not only related to the DOR. He said the comment on no more business as usual is something the subcommittee needs to take a look at. The contracting state has a bad record with contracts for information technology projects and this goes back to SABHRS and the problems that system had not too long ago. He also talked about a budget system that was worked on by the executive office and LFD. This budget system was a failure. He felt that there needs to be a different way to go about these contracts and it will be important to have quality assurances. The contractor needs to be more liable and responsible for what they implement. **Mr. Schenck** said there were two issues that need to be focused on. One, is the governance of information technology (IT) in general and the second is how the state contracts for IT system development. There is no teeth in how the state manages IT from a central basis and the departments can go off and do their own things. A study is of IT contracting is needed. **Rep. Lindeen** asked if **Mr. Schenck** recommended the study of IT contracting is needed to the Legislative Finance Committee would it get done? **Mr. Schenck** said the legislature puts out a number of resolutions to get studies funded specifically. The finance committee has work plans and he is committed to getting this done. He said he can not guarantee, but felt it would be if the legislature felt the need for it to be done.

Chairman Davies called on **Debbie Hitt, an employee of St. Peter's Hospital in the intensive care unit** because she has been involved in a new computer system implementation. **Mrs. Hitt** found the testimony very interesting because of similar problems experienced under similar circumstances at St. Peter's while implementing a new computer system. One of the things she would strongly suggest is that DOR reconsider doing parallel runs. Any time a new system is started its important to compare how the new system works with how the old system worked. You can not compare a new system to itself. The excuse that is always given for a parallel system is its too costly, because everything has to be done twice. However its very costly if the system breaks down.

Chairman Davies made a comment that the legacy systems were not kept up and running along with POINTS phase I and he had the idea that this happened because it was not Y2K compatible. **Mr. Miller** said one of the eight legacy systems that was replaced by POINTS apparently Y2K compliant. That was just one of eight and the rest were not. DOR determined it was not cost effective and DOR thought it would be a throw-away cost. **Mr. Miller** said they will research the numbers associated with the cost of running

parallel and the cost to keep legacy systems and make them Y2K compliant.

Mr. Alme reiterated two things and one was to include DOR in the subcommittee's discussion to the extent possible, because he is ultimately responsible for what happens in their department. He said the second thing that he would ask is an opportunity for DOR to get information to the subcommittee, because there have been a lot of things said in the hearing and a lot of information since his been there. There are basically a lot of rumors. Some are true and some are not. Before the subcommittee ends he wanted them to be aware of the facts and also to allow DOR to confirm these facts. He offers his department's cooperation in any way and wants to get the DOR in a position for it to realize the best that it has done and best it can achieve going forward.

Chairman Davies asked that the DOR go over the Legislative Audit report item for item. He asked for the audit to be under way as soon as possible. The audit can not be done until late summer because the Legislative Audit Division is currently engaged in other audits. **Mr. Alme** asked if the Legislative Audit Division has any opening to fit the DOR in for an audit that they do so, but for now its scheduled for July.

JOINT APPROPRIATIONS SUBCOMMITTEE ON GENERAL GOVERNMENT AND
TRANSPORTATION

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ADJOURNMENT

Adjournment: 11:45 A.M.

REP. BOB DAVIES, Chairman

CYNDIE LOCKETT, Secretary

BD/CL

EXHIBIT (jgh32aad)